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REPORT OF THE EXTERNAL AUDITOR, FINANCIAL PERFORMANCE REPORT AND PROGRAMME PERFORMANCE REPORT FOR THE BIENNIUM 1992-1993

Comments of the Director-General on the report of the External Auditor

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Introduction

1. The Director-General, in presenting his comments on the report of the External Auditor covering the period 1992-1993 (IDB.13/7-PBC.10/8), would like to acknowledge, with thanks, the observations and constructive recommendations made in the report. The Director-General also wishes to record his appreciation for the excellent work of the External Auditor since his initial appointment in 1986. The high standards of the External Auditor and his officers have contributed in no small measure to the work of UNIDO. As in previous bienniums, the External Auditor has conducted a detailed examination of the accounts and activities of UNIDO, particularly in the areas of financial management, purchasing and contracting, electronic data processing, evaluation of technical cooperation activities and personnel matters. The Director-General noted with appreciation that comments of the Administration are included in the External Auditor's report. The present document provides additional comments on the items requiring special attention under the main audit activity groupings contained in the report of the External Auditor.

I. SPECIFIC COMMENTS

Budgetary, accounting and financial reporting procedures
(paras. 7-18 and 43-95)*

Regular budget assessed contributions income
(paras. 7 and 43-46)

2. The information presented in the report of the External Auditor on the status of assessed contribution payments for the bienniums since UNIDO became a specialized agency in 1986 demonstrates the magnitude of the problem faced by the Secretariat in the planning and management of financial resources, caused by the late or non-payment of assessed contributions. The improvement in the percentage of unpaid assessments in 1990-1991 over 1988-1989 was unfortunately not maintained in 1992-1993. The Director-General is confident that Member States will demonstrate their support for the Organization by meeting their financial obligations in full in due course, thereby reducing the high level of unpaid assessed contributions.

Regular budget implementation
(paras. 8 and 47-50)

3. The unutilized balances of appropriations in 1992-1993 result from conservative financial policies applied by the Secretariat which were

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* Paragraph numbers refer to paragraphs in the report of the External Auditor (IDB.13/7-PBC.10/8).

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implemented to ensure that, at all times during the biennium, the Organization maintained sufficient cash to meet outstanding obligations.

4. A substantial portion of the unutilized balances arise as a direct consequence of the uneven pattern of payment and of the high level of unpaid assessed contributions, described in paragraphs 43 to 46 of the External Auditor's report. Uncertainties in respect of the receipt of assessed contributions severely undermine the proper planning of financial implementation and lead to forced expenditure reductions.

5. The measures taken by the Secretariat during 1992-1993 were a direct response to Member States' demands that expenditures should remain within available cash resources. These measures also endeavoured to respond to the call by Member States for 15 per cent of appropriations to be kept in reserve pending receipt of assessed contributions (resolution GC.4/Res.27).

6. Other than the maintenance of higher-than-budgeted vacancy factors and reductions in staff travel that reduced costs in all departments, the measures introduced by the Secretariat in response to Industrial Development Board decision IDB.11/Dec.30 (e) were mainly directed to administrative and general operating costs. The Secretariat was able to ensure that the Regular Programme of Technical Cooperation was implemented in full.

7. The improvement in the cash resource base under the regular budget should result in a lower level of unutilized balances in the 1994-1995 biennium. In its endeavours to maximize financial implementation, the Secretariat remains dependent on the payment by Member States of their assessed contributions on a timely basis.

Regular budget unliquidated obligations
(paras. 9 and 51-55)

8. The Director-General agrees with the recommendations of the External Auditor to take additional measures to ensure compliance with the legislative requirements regarding regular budget outstanding obligations review and reporting, and the administrative instruction (UNIDO/DA.71) defining designation and functions of certifying officers will be expanded to include, pursuant to financial regulation 4.2 (c), the responsibility of certifying officers for the review of unliquidated obligations.

Regular Programme of Technical Cooperation
(paras. 10 and 56-58)

9. The Director-General has noted the comments of the External Auditor and advises that very careful attention has been given to compliance with financial regulation 4.2 (a) and (b) and with financial rule 104.1 to ensure that unliquidated obligations in respect of the Regular Programme of Technical Cooperation at the end of the 1992-1993 biennium accurately reflect charges for goods supplied and services rendered during that biennium.

Commitments approved for further fiscal periods
(paras. 11 and 59-64)

10. The Director-General has taken note of the comments and recommendations of the External Auditor in respect of the system for recording of and accounting for commitments for future bienniums. As stated by the External Auditor in paragraph 62 of his report, an amendment to the Financial Rules of UNIDO will be proposed to bring legislative provision into line with actual practice, and Financial Services will give attention to the introduction of a reliable system for the recording and accounting of commitments for future bienniums.

Gains/losses on exchange
(paras. 12 and 65-66 and annex I, paras. 1-30)

11. In line with the recommendation of the External Auditor, the Director-General will propose an amendment to financial rule 110.7 in order that legislative provision reflect actual practice in the accounting and reporting for gains/losses on exchange.

Operational budget implementation
(paras. 13-14 and 67-74)

12. The Director-General acknowledges the importance of the issues raised by the External Auditor in respect of the mandatory operational budget reserve.

13. The mandatory level of the reserve was effectively lowered during the 1992-1993 biennium to permit the financing of the deficit in the operational budget resulting from the excess of expenditure over income.

14. As noted by the External Auditor, the purposes of the mandatory operational budget reserve, which is described as a contingency reserve in the financial statements, are not clearly documented. The operating reserve, which has been a part of the UNIDO operational budget since the Organization became a specialized agency in 1986, was previously governed by United Nations administrative instruction ST/AI/286, which described the purposes of the reserve. The reserve was intended to protect the Organization against unforeseen shortfalls in delivery, inflation and currency adjustments, or to provide for legal obligations arising from abrupt termination of activities.

15. The Director-General intends to respond to the recommendation of the External Auditor on this matter by submitting policy guidelines for the utilization of the mandatory operational budget reserve to the Programme and Budget Committee at its eleventh session. The report will also make recommendations on an appropriate level for the reserve and include a plan for the restoration of the reserve balance.

Tax Equalization Fund - Treatment of accounts receivable
(paras. 15 and 75-78)

16. The Director-General takes note of the comments of the External Auditor on the Tax Equalization Fund and the tax reimbursement agreement between UNIDO and the Government of the United States of America and the amount due from the Government of the United States of America in respect of reimbursement of taxes levied on United States citizens during the period 1986 to 1991. A report on the status of the negotiations by the Director-General with the Government of the United States will be presented to the Programme and Budget Committee at its eleventh session.

Unliquidated obligations - UNDP operating fund
(paras. 16 and 79-84)

17. The Director-General is pleased to note the observations of the External Auditor on the substantial decrease in the value of unliquidated

obligations as well as the number of field inter-office vouchers remaining unprocessed at year-end, compared with the corresponding values for previous years.

18. The Director-General agrees with the recommendation that the same procedure will be made applicable to future reviews of technical cooperation obligations as already applied to those of the regular and operational budgets.

Advances for seminars and study tours for technical cooperation activities
(paras. 17 and 85-90)

19. Although the Secretariat considers that the present method of accounting and recording of advances properly meets reporting requirements, consideration will be given to the recommendation of the External Auditor to amend UNIDO accounting practice to bring it into line with generally accepted accounting standards.

Bank reconciliations
(paras. 18 and 91-95)

20. The Director-General shares the deep concern of the External Auditor regarding bank reconciliations. The Accounts and Payments Unit, responsible for this function, is suffering from very severe staff constraints, as noted by the External Auditor. The Unit was obliged to establish priorities to meet statutory obligations to UNIDO staff and to external donors, as a result of which some functions had to be deferred. Action has been initiated to address the staffing problem and priority will be given to the outstanding reconciliation of bank accounts.

Contracts and purchases

Written policies and procedures
(paras. 19 and 96-99)

21. The guidelines contained in the new terms of reference of the Committee on Contracts (UNIDO/DG/B.22/Rev.1) have been helpful for the preparation of submissions to the Committee on Contracts and for the interaction between the substantive units and the Purchase and Contracts Units. Management agrees with the view of the External Auditor that it is desirable to accelerate the finalization and issuance of the manual on policies, procedures and rules governing the activities of the Purchase and Contracts Branch. While it will be necessary to review the existing draft text in the light of the restructuring of the Secretariat and to take into account the reduced staffing level, it is considered that the manual should be finalized and issued without awaiting the completion of new financial rules for UNIDO.

The roster of vendors and the roster of industrial consultants
(paras. 20 and 100-104)

22. The observation in paragraph 100 that in many instances the number of bidders invited was too limited and the response rather poor is based on a review of the submissions to the Committee on Contracts in the period 1986 to 1992. It should be noted, however, that the situation has improved with the establishment and development of the computerized databases of vendors and consulting firms. These rosters have become the most important tools for the selection of potential vendors and contractors and staff are no longer restricted to information gleaned from catalogues and similar printed sources. The recommendations that the rosters be revitalized and updated, and that a procedure be established to constantly identify new potential vendors and contractors, are noted and accepted. In fact, as noted by the External Auditor, the roster of consulting companies was updated during the period under review and, in respect of the roster of vendors, action has been taken to regularly access potential new vendors by merging the database of the Inter-Agency Procurement Services Office (IAPSO) with the UNIDO vendors' roster. As maintenance of the rosters must be a continuous process, it is intended to establish a schedule for updating the rosters.

23. The information referred to in paragraph 102 regarding the lack of use of the rosters by the Purchase Unit was obtained before the last quarter of 1993. In this respect, it should be noted that the vendors roster remains in need of further refinement in order to make it even more useful. In particular, it is pointed out that certain items procured by UNIDO for its technical cooperation projects are so specific that it is difficult to identify vendors by using the United Nations Common Coding System. This is gradually being resolved by IAPSO. In addition, the user-friendliness of the vendors roster has been enhanced by Management Information Services (MIS) in consultation with the Purchase Unit. Regarding purchases for Headquarters, the Secretariat would emphasize that the vendors for these purchases are also rostered and that the purchasing officers should be encouraged to use the existing computerized roster as much as possible. Careful consideration will be given to the suggestion by the External Auditor to require that the relevant roster be used as a matter of normal procedure and to record the code numbers in the case file.

The management of purchase and contracts files
(paras. 21-22 and 105-116)

24. Concerning the External Auditor's observations in paragraphs 105 to 110, it is recalled that in accordance with financial rule 109.19, contracts may be awarded without inviting bids or calling for proposals, inter alia, when the proposed contract involves a commitment of less than $20,000 provided that the award is made after an assessment of competitive quotations, based on conformity with specifications, delivery schedules and prices or comparative prices, where available. The Secretariat agrees that such competitive quotations might be obtained from procurement catalogues and databases that provide current prices and that the case file should contain a written record of the competitive quotations assessed and not merely a reference to the applicable financial rule. Action will be taken to ensure compliance with this procedure. The specific observations in paragraph 111 have been duly noted. It is hoped that the introduction in the near future of phase one of the computerized requisition, purchase and contract system will facilitate the proper and timely preparation of requisitions. The requirement that the acknowledgement copy of the purchase order be returned by the vendor is very important for the reason mentioned by the External Auditor and action will be taken to ensure compliance by vendors in all cases. The receiving and inspection reports are not always received from the projects, although it is always requested as per copy 8 of the purchase order, which is forwarded to the project concerned. A note recalling this important requirement will be addressed to UNIDO field offices. Regarding the evaluation of the performance of equipment vendors, in the process of future computerization consideration will be given to the inclusion

of fields to record receiving and inspection reports.

25. The few inaccuracies detected by the External Auditor in the administration of the contract files have been duly noted. At the same time, it is recalled that the Contract Management Information System is a very extensive computerized information system and that it is not the only tool available to the contract officers.

Contract for the provision of travel agency services
(paras. 23 and 117-119)

26. According to the observations of the External Auditor, formal competitive bidding with published advertisement should have been used to select the company to which the contract for the provision of travel services was awarded. As noted by the External Auditor, the selection was made on the basis of requests for proposals that had been sent to seven companies, as is the usual procedure for contracts. Management is of the view that this action was in conformity with financial rule 109.18 (a), which mentions the invitation of tenders for bids by advertisement only as an option, not as a requirement. The draft manual on policies, procedures and rules for the activities of the Purchase and Contracts Units would require advertisement as a normal procedure for very large contracts, but since the manual has not yet been issued, it could not be considered binding. For the same reason, it would not necessarily have made a difference whether the value of the contractual commitment had been considered to include the refunds made by UNIDO to the company for tickets ordered or merely the fee paid to the company for its own services. The views expressed by the External Auditor have been noted, however, and will be taken into account in the final version of the above-mentioned manual.

Technical cooperation

Project expenditure - financial information
(paras. 24 and 120-124)

27. The Director-General notes the comments of the External Auditor and wishes to advise that action has been taken to ensure the maximum mobilization of funds for technical cooperation activities. Information on developments in this respect is provided in documents IDB.13/4-PBC.10/5, IDB.13/9-PBC.10/11, and - as noted by the External Auditor - the Annual Report of UNIDO, 1993 (IDB.12/2-PBC.10/2, chap. VIII, paras. 10-23, and chap. III, paras. 86-101).

Financial completion of projects
(paras. 25 and 125-133)

28. The Secretariat will take steps to ensure that, wherever feasible, the significant improvement in the financial completion of projects, as noted by the External Auditor, is further enhanced.

Field audits
(paras. 26-28 and 134-139)

29. The Secretariat agrees with the conclusions of the External Auditor, but in respect of Indonesia wishes to point out that despite a programming mission in December 1988, a project identification and formulation mission in 1990, and the preparation of a country strategy paper in 1993 together with the preparation of several TSS-1 proposals since 1991, UNIDO efforts have regrettably generated little impact on the UNDP programming mechanism.

30. With respect to the observations on project management, the Secretariat concurs with the points raised and has undertaken the necessary measures to address the shortcomings referred to.

Electronic data-processing systems

Financial information
(paras. 29 and 140-145)

31. The Director-General takes note of the statement of the External Auditor indicating that the electronic data-processing (EDP) costs stayed within the budgeted resource requirements and confirms that financial implementation was kept under close review and that savings and cost reductions in non-staff costs were made wherever possible. While savings were also achieved in staff costs through the maintenance of vacancies, this resulted in a less effective implementation of the EDP programme as a whole and in some underutilization of equipment and software.

Distribution of EDP non-staff costs
(paras. 30 and 146-149)

32. The Director-General agrees with the observation of the External Auditor that the charge-back system for EDP non-staff costs has been used in the budget document for presentation purposes only, to indicate the degree of mainframe utilization and the distribution by division of end-user equipment and software.

33. In order to charge the United Nations Office at Vienna for mainframe utilization, reports are run by MIS that distribute mainframe usage by organizational unit, within and outside UNIDO. This information can be used as the basis to charge-out mainframe costs. A first step in the direction of allocating resources and assigning responsibility for the utilization of such resources at the major programme level was made in the 1992-1993 biennium for desktop equipment and related software.

34. A condition of distributed (or decentralized) computing is the decentralization of planning, budget and control. As UNIDO gradually moves towards distributed processing, a charge-back system will become meaningful. The ultimate goal is to implement a charge-back system for non-staff expenditures, beginning with a distribution of budget resources for office automation and network in the 1996-1997 budget.

A system for managing, controlling and auditing automation projects (SMCA)
(paras. 31 and 150-154)

35. The Secretariat agrees with the External Auditor that his examination of the requisition, purchase and contracts system shows weaknesses in the implementation of the systems development methodology, which require improvement.

36. The procedures to be approved by the Information Technology Steering Committee (ITSC) indicate that only those systems will be implemented where the end-user agrees to commit the necessary resources to the analysis as well as to the review of the design of a system. The above, together with the contribution of the divisional information managers, and a high priority being placed on quality review in MIS, will all contribute to enhancing the quality of any future systems development.

37. The Director-General takes note of the statement of the External Auditor that, in spite of staff limitations, the Applications Services Unit made all possible efforts to try to comply, as much as possible, with the various user demands regarding automation projects.

Formal standards concerning end-user computing
(paras. 32 and 155-158)

38. As a first measure towards establishing standards and guidelines for end-user computing, ITSC recommended to take stock of existing personal computer (PC) applications. The division information managers have now been appointed and will take on the task of preparing the inventory of PC applications and databases for their divisions, based on a standard form prepared by MIS. In the course of 1994 the information for the whole organization will be summarized by MIS and included in the applications portfolio of mainframe applications. Subsequent to this, the division information managers, in cooperation with MIS, will work on the preparation of standards and guidelines for the development and documentation of future PC applications.

Providing back-up for key users
(paras. 33 and 159-161)

39. A permanent solution for adequate back-up of staff in charge of mission-critical applications can only be found in the context of the 1996-1997 budget and will be taken into consideration at the time the budget submission is prepared. In the meantime, while recognizing staffing constraints, it is worth mentioning that MIS has staff members in charge of other duties in MIS, with sufficient experience in the maintenance and running of major applications. In case of an emergency such staff could be redeployed temporarily to ensure continuity of operations and sufficient support for mission-critical applications.

Personnel matters

Financial information on the staff costs of substantive departments of UNIDO
(paras. 162-163)

40. The Director-General has noted the comments of the External Auditor and the information provided in table 20 of his report.

The organizational structure of UNIDO
(paras. 34 and 164-178)

41. The Director-General has taken note of the report on the main organizational changes during the period 1986 to 1992 and of the analysis of selected organizational components. As pointed out by the External Auditor in his report, the structure has been subject to continuous review and has involved extensive consultations with policy-making organs. The underlying reasons for such organizational changes were to bring the various organizational units into line with the operational functions of UNIDO.

42. The Director-General does not wish to comment in detail on previous reorganizations, considering that they have been superseded by the reorganization approved at the fifth session of the General Conference. However, the observations and comments of the External Auditor will be taken into account in future exercises of this nature.

The 1993 staff reduction exercise
(paras. 35 and 179-185)

43. The staff reduction exercise was conducted in accordance with the UNIDO Staff Regulations and Rules, and with the policy for reassignments, abolition of posts and staff reductions as outlined in Director-General's Bulletin UNIDO/DG/B.169 and Add.1.

44. Whereas the Staff Regulations and Rules of UNIDO are sufficiently clear on the entitlements of staff members whose appointments are being terminated, a certain degree of flexibility is essential in order to facilitate negotiations with staff. While an element such as the period of notice for staff holding fixed-term appointments might be adapted through appropriate administrative circulars to take account of General Assembly resolution 37/126 concerning staff members with over five years of service, the Director-General would prefer to keep the existing rules and regulations intact.

45. In paragraph 17 of Director-General's Bulletin UNIDO/DG/B.169 it was stated that staff members on fixed-term contracts would not necessarily be at a disadvantage during the course of the staff reduction exercise. It should be noted that a significant proportion of those staff members extended between August 1993 and January 1994 had more than five years of service with UNIDO. In addition, the appointments of other staff members on fixed-term appointments were extended during this period based on recommendations made earlier in 1993, at which time a final decision on a staff reduction exercise had not yet been made.

46. Extensive consultations with department heads and managers took place throughout the exercise in an effort to ensure that the fixed-term staff being retained were considered essential and constituted a valuable core of skills necessary for the future programmes of UNIDO.

47. While the non-extension of more fixed-term appointments might have seemed appropriate in the short term, it would have had negative consequences for the high quality staff requirements of the rejuvenated Secretariat. Cognizant of the financial constraints facing the Organization, however, from November 1993 the Secretariat limited the period of extension for fixed-term staff members to between six months and two years.

Staff mobility and rotation
(paras. 36 and 186-188)

48. Every effort is made by the Organization to encourage its staff to apply for field posts and other such assignments. However, being a relatively small organization with only a limited number of offices outside Headquarters, there are certain limits to the scope of field assignments for UNIDO staff. In reorienting the UNIDO policy on field representation, additional emphasis is being placed on increasing the number of headquarters staff members being posted to UNIDO Country Director offices. In addition, further efforts will be made to increase the number of staff members detailed to technical cooperation projects.

49. While service in the field is one of several factors that is taken into consideration for promotion purposes, other factors such as quality of performance, availability of posts and seniority are also involved.

Representation of women in the Secretariat
(paras. 37 and 189-192)

50. The 1993 promotion review for Professional-level staff was postponed to 1994 owing to the staff reduction and reorganization exercises undertaken in 1993. The number of female staff members included in the 1993 promotion register will bring the total number of women at the P-5 level and above to ten, thus restoring the balance achieved at the end of December 1992.

51. This notwithstanding, it is understood that further efforts will have to be made by the Secretariat to ensure that the proportion of women at the senior Professional levels is increased in line with the targets established by the policy-making organs.

Recruitment of consultants
(paras. 38 and 193-196)

52. Special attention will continue to be given to the justification on the choice of a particular consultant.

53. The provisions of United Nations administrative instruction ST/AI/296/Add.1 concerning consultants and participants in advisory meetings are being applied by UNIDO. The Director-General will ensure that this administrative instruction is revised to include a lump sum remuneration option, including travel if appropriate. The cost of such travel would be calculated on the basis of the pertinent provisions of the staff rules.

Performance appraisal report
(paras. 39 and 197-203)

54. The Director-General has noted with interest the comments of the External Auditor concerning the performance appraisal report. It is the firm intention of the Director-General to improve the existing system and a working group is being established to that effect.

Home leave travel
(paras. 40 and 204-208)

55. The Director-General will take the observations concerning home leave travel into account when reviewing the current arrangements for implementing the system of the home leave entitlement for UNIDO staff.

General conclusions and recommendations
(paras. 41 and 209-212)

56. It is anticipated that the needs of those organizational units referred to by the External Auditor will be addressed by the Director-General in the programme and budget proposals for the 1996-1997 biennium. In the interim, redeployment of financial and staff resources and recruitment action will be considered in order to maintain an adequate level of essential services.

57. The Director-General will take into account the recommendations of the External Auditor concerning staffing review and an independent staff inspection function. These proposals will require further study, including the possible use of external consultants.

58. While the suggestion that the contracts of Professional-level staff in the substantive divisions be limited to a maximum of eight years might be a useful option for staff at the Director level, its application to other categories of staff would require further scrutiny. If such a policy were to be adopted, it would be important that the Director-General not be deprived of the possibility of retaining staff members beyond eight years if the exigencies of the service so required. A general rule limiting the service of substantive staff to eight years of service might be regarded as being at variance with General Assembly resolution 37/126 and would also create additional problems of competitiveness in the recruitment and retention of staff. Nevertheless, the option will be considered seriously.

Other matters

Draft finance manual
(paras. 42 and 213-215)

59. The Secretariat will take steps to finalize and publish the amended Financial Regulations and Rules of UNIDO, following which the draft finance manual of UNIDO will be re-reviewed, amended as appropriate, and published.

Amounts written off, cases of fraud or presumptive fraud, and ex-gratia payments
(paras. 216-217)

60. With respect to the possible write-off cases referred to by the External Auditor, these have already been submitted to the Internal Auditor pursuant to financial rule 109.14.

II. ACTION REQUIRED OF THE COMMITTEE

61. The Committee may wish:

(a) To express its appreciation and thanks to the Senior President of the Audit Office of Belgium and his officers for the most valuable contribution made to improving the financial management and control of UNIDO during the period 1986 to 1994;

(b) To take note of the Director-General's comments (IDB.13/8-PBC.10/9) on the report of the External Auditor for the biennium 1992-1993 and of the action taken in response to the observations and recommendations of the External Auditor.